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No. 95-2078

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1995

SPRING MEADOWS APARTMENT COMPLEX, LIMITED PARTNERSHIP,

Petitioner,

vs.

DAVID L. STALLINGS and BARBARA J. STALLINGS,

Respondents.

On Petition for Writ of Certiorari to the Arizona Supreme Court

REPLY BRIEF FOR PETITIONER

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Petitioner Spring Meadow Apartment Complex Limited Partnership replies to Respondents' Brief in Opposition and requests that the Petition for Writ of Certiorari be granted.

I. THIS COURT SHOULD GRANT CERTIORARI BECAUSE THE ARIZONA SUPREME COURT EXPRESSLY INTERPRETED UNSETTLED FEDERAL BANKRUPTCY LAW.

As set forth in the Petition, the federal circuits and the state courts of last resort which have addressed the issues in this case are hopelessly split as to their proper resolution. Moreover, practitioners and judges frequently encounter these issues and apply inconsistent analyses. It is time this Court put an end to the confusion and inconsistency.

Rather than address the merits of the unsettled issues of federal law the Petition raises, Stallings attempt to avoid them by claiming this Court lacks jurisdiction because Spring Meadows allegedly has failed to raise any important unresolved question of federal law. This is incorrect. The Arizona Supreme Court in *Stallings* expressly interpreted federal bankruptcy law and 11 U.S.C. § 362 regarding the effect of a violation of the § 362 automatic stay. In its opinion, the Arizona Supreme Court interpreted the Ninth Circuit's holding in *In Re Schwartz*, 954 F.2d 569 (9th Cir. 1992), interpreted § 362's "annulment" provision, analyzed the legislative history and the 1978 Revision Notes behind § 362, held that the void versus voidable issue is irrelevant and interpreted the circumstances under which § 362(d) stay relief is appropriate.[1]

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1. Stallings' suggestion that the "primary issue" the Arizona Supreme Court addressed was "whether the statute of limitations was equitably tolled under Arizona law" is incorrect. The Arizona Supreme Court did not even address this issue. Rather, the Court asked the parties to address this

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The Arizona Supreme Court thus did not merely rely on the bankruptcy court, but independently interpreted these issues itself. Indeed, the Arizona Supreme Court Chief Justice explicitly stated at the oral argument that Arizona courts have the right and authority to interpret federal bankruptcy law independently of other federal courts:

> Let's get one thing out of the way. I just finished testifying in Congress that we were not bound by the Ninth Circuit decisions. Now tell me why I was wrong. Maybe I'd better write a letter.
>
> * * *
>
> [T]his Court has equal authority with the Ninth Circuit and the United States District Court to decide questions of federal law subject only to revision by the United States Supreme Court.

Appendix J, 73a, Petition for Writ of Certiorari.

Further evidence that the Arizona Supreme Court independently interpreted § 362 and did not just rely on the bankruptcy court's interpretation is that the Court concluded its opinion by noting that the bankruptcy court's ruling was "in harmony" with its own interpretation. If a state court chooses to exercise judicial review as to a federal statute, that court's interpretation is subject to this Court's review.

Moreover, the effect of a violation of § 362's automatic stay

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(Cont'd)

alternative issue by way of supplemental briefing, but never reached the issue because of the Court's interpretation of federal law.

is not a question of state law, but of federal bankruptcy law. It is not state law, but rather § 362's express prohibition against pursuing claims against debtors in bankruptcy, which renders ineffective actions filed in violation of the stay. Similarly, 11 U.S.C. § 108(c)'s savings provision extending the statute of limitation governs whether actions filed in violation of the stay must be refiled after stay relief is granted. Sections 362 and 108(c) thus clearly preempt state law and are at issue here.

Stallings' argument that this Court lacks jurisdiction also because Spring Meadows did not appeal from the bankruptcy court's June 1991 order lifting the stay and the December 1994 order of clarification retroactively annulling the stay is both factually and legally incorrect. First, Spring Meadows did not appeal from the June 1991 order because it did not retroactively annul the stay. There was thus no reason for Spring Meadows to appeal from that order.

In addition, Stallings fail to mention that Spring Meadows was prevented from directly appealing from the December 1994 bankruptcy court order retroactively annulling the stay because neither Spring Meadows nor its counsel was sent a copy of the order. As set forth in the Petition, Spring Meadows thus filed a motion pursuant to Bankruptcy Rule 9024 seeking to have the bankruptcy court both correct and re-enter its December 1994 order. The bankruptcy court denied that motion, and Spring Meadows is appealing from that denial in the federal courts.

More importantly, Stallings' argument that this Court lacks jurisdiction is also logically incorrect. In its Petition, Spring Meadows seeks review of the Arizona Supreme Court's decision, not the bankruptcy court's order. As discussed above, the Arizona Supreme Court independently and explicitly interpreted federal law governed by § 362 and § 108(c) of the Bankruptcy Code regarding the effect of a violation of the automatic stay and the appropriateness of retroactive stay relief.

Stallings' claim that all the Arizona Supreme Court did was to apply the bankruptcy court's order is thus clearly incorrect.

Even if the Arizona Supreme Court had not interpreted federal bankruptcy law, but only the bankruptcy court's orders, its interpretation was incorrect. Stallings' argument that the bankruptcy court's June 1991 stay lift order constituted a retroactive annulment is unsupported. The June 1991 order merely "lifted" the stay and permitted Stallings' "claims," not their pending action, to proceed. That order did not grant "retroactive" relief, "annul" the stay or permit Stallings to ignore § 108(c)'s requirement to refile the action. In addition, the form of order which the bankruptcy court signed in June 1991 was provided by Stallings. Thus, any ambiguity as to whether it ordered a retroactive annulment should be construed against Stallings, which drafted the form of order. *See United States v. Seckinger, Trading As M.O. Seckinger Co.*, 397 U.S. 203, 210-11, 90 S. Ct. 880, 884-85, 15 L. Ed. 2d 224 (1979); *Sutter Home Winery, Inc. v. Vintage Selections, Ltd.*, 971 F.2d 401, 406 (9th Cir. 1992) (ambiguities in a document are to be construed and resolved against the drafter).

In addition, the surrounding record on which Stallings rely does not support their claim that they "unequivocally" sought retroactive relief. To the contrary, nowhere did Stallings' 1991 Motion for Relief from Automatic Stay seek retroactive relief or annulment or set forth *any* grounds supporting such extraordinary relief.

Stallings' interpretation of the bankruptcy court's June 1991 order based on a dictionary definition of "annul" is also incorrect because it ignores case law and commentators which have interpreted § 362. These authorities have repeatedly interpreted § 362's "annul" language as *the* provision authorizing retroactive stay relief. *See* cases cited in Petition for Writ of Certiorari, at 13. Numerous cases have also held that a "lifting"

of the stay is prospective, not retroactive. *See In Re Albany Partners, Ltd.*, 749 F.2d 670, 675 (11th Cir. 1984); *Ellis v. Consolidated Diesel Elec. Corp.*, 894 F.2d 371, 373 (10th Cir. 1990). The Arizona Supreme Court thus clearly interpreted federal bankruptcy law contrary to the weight of authority.

This case thus raises important and unresolved questions of federal law which the Arizona Supreme Court undisputedly interpreted here.

II. BOTH FEDERAL AND STATE COURTS ARE HOPELESSLY DIVIDED REGARDING THE PROPER PROCEDURE FOR ADDRESSING A VIOLATION OF THE AUTOMATIC STAY.

Stallings attempt to prevent this Court from addressing the "void versus voidable" debate by claiming it is irrelevant. Stallings' argument ignores the overwhelming majority of cases which begin their analysis regarding the proper procedure when an action is filed in violation of the automatic stay by determining whether such violations are void or voidable. *See* cases cited in Petition for Writ of Certiorari, at 17-21. Even Stallings' own Brief in Opposition cites to numerous cases using the void or voidable analysis. *See* Stallings' Brief in Opposition, at 13-15, fn. 5-6. Thus, to claim that the void versus voidable issue is irrelevant, when virtually all cases use it as the first step in their analysis, is incorrect.

Moreover, though the Arizona Supreme Court claims that the Ninth Circuit's decision in *In Re Schwartz*, 954 F.2d 569 (9th Cir. 1992) suggests that the void versus voidable issue is inapplicable if retroactive stay relief is granted, this is the only case Stallings cite in support of this argument, which is contradicted by the majority of cases. At a minimum, this conflict desperately needs resolution.

Stallings' argument based on *Easley v. Pettibone*, 990 F.2d 905 (6th Cir. 1993) is both factually incorrect and contradicts *In Re Schwartz*. Stallings' claim that in *Easley* the bankruptcy court denied retroactive relief is clearly incorrect. The true facts are that the bankruptcy court *granted* retroactive relief, though the Seventh Circuit eventually reversed that order. *Id.* at 907. Moreover, Easley expressly criticizes the Ninth Circuit's *In Re Schwartz* opinion on which the Arizona Supreme Court relied, thus confirming the existence of a conflict in the circuits.

Finally, Stallings' claim that Spring Meadows' "obsession" with the void versus voidable issue "has as the air of scholastic about it" ignores the fact that numerous cases cited by both parties use the void versus voidable analysis. It is those cases which have created an otherwise irreconcilable conflict which only this Court can resolve. Thus, the Arizona Supreme Court's reliance on an isolated case which holds that the void versus voidable distinction is irrelevant merely underscores the fact that this Court needs to address this issue.

III. THIS COURT ALSO SHOULD GRANT CERTIORARI AS TO THE IMPORTANT UNRESOLVED ISSUE OF WHEN RETROACTIVE RELIEF FROM THE § 362 STAY IS APPROPRIATE.

Stallings attempt to prevent this Court from considering an even more important and unresolved issue than the "void versus voidable" debate — That is, when is retroactive relief from § 362's automatic stay provision appropriate? As discussed in the Petition, this issue has not been squarely addressed, though numerous courts generally recognize that such extraordinary relief should be granted only in limited circumstances. *See* cases cited in Petition for Writ of Certiorari, at 23-24.

Stallings again argue that this Court should not consider this issue because Spring Meadows did not oppose Stallings' 1991

Motion for Relief from the Automatic Stay or appeal from the bankruptcy court's June 25, 1991 stay lift order. Again, as discussed above, there was no need to challenge this motion or order because they did not seek or grant retroactive annulment, much less set forth any grounds justifying it.

When Stallings finally did belatedly seek retroactive stay relief three and one-half years later in 1994, Spring Meadows promptly opposed Stallings' request for the same reasons raised here. Any delay in this case is thus not due to Spring Meadows, but to Stallings who waited three and one-half years after learning they had violated the bankruptcy stay to seek retroactive relief. Stallings thus cannot accurately or equitably complain that Spring Meadows did not act properly.

Stallings improperly rely on *Grella v. Salem Five Cent Savings Bank*, 42 F.3d 26, 34 (1st Cir. 1994) for the proposition that "the only issue properly and necessarily before a bankruptcy court during relief from stay proceedings is whether the movant creditor has a colorable claim." While it is true that *Grella* holds a claimant must meet the minimal hurdle of having a colorable claim in order to obtain prospective stay relief, *Grella* does not involve retroactive annulment. As indicated by the cases cited in Spring Meadows' Petition, a much higher standard is required for retroactive annulment.

Stallings also claim that their ignorance of the bankruptcy stay when filing the complaint justified the granting of retroactive stay relief. Stallings reliance on several cases for this proposition is misplaced and misconstrues those authorities. *In Re Jones*, 63 F.3d 411 (5th Cir. 1995) supports Spring Meadows', not Stallings', argument. Jones issued a promissory note securing real property. When Jones defaulted on the note and the note holder attempted to foreclose on the property, Jones filed a bankruptcy petition. The parties attempted to resolve the matter and Jones withdrew the bankruptcy petition, only to default

again. The note holder again accelerated on the note and set a foreclosure sale. Jones refiled their bankruptcy within a very short time after withdrawing their previous bankruptcy and never notifed the note holder regarding it. The sale of real property was accomplished without Jones ever notifying the note holder of the bankruptcy. The Fifth Circuit refused to invalidate the sale because of Jones' failure to notify the note holder of the second bankruptcy during the course of the foreclosure sale. *Id.*

Jones does not support Stallings' simplistic statement that retroactive relief is permitted when the claimant has no notice of the bankruptcy stay. If this were true, retroactive relief would be appropriate in almost every case since most actions filed in violation of the bankruptcy stay are filed without actual knowledge of the stay. Instead, *Jones* supports Spring Meadows' argument that retroactive relief is appropriate if the debtor either abuses the bankruptcy process by multiple filings or hides the fact of its bankruptcy from the claimant, both of which happened here.

Similarly, *Franklin Savings Association v. Office of Thrift Supervision*, 31 F.3d at 1020, 1023 (10th Cir. 1994) again supports Spring Meadows' position. First, this case contradicts Stallings' argument that "11 U.S.C. § 362(d) makes no distinction between the grounds required to obtain relief from the automatic stay," including retroactive relief. Brief in Opposition, at 19. *Franklin Savings* makes clear that there is a distinction between retroactive annulment and prospective stay relief. In that case, the court refused to grant retroactive annulment because the circumstances there did not justify it. Indeed, Stallings parenthetically quotes the court out of context when it states that retroactive relief is appropriate when "claimants are 'honestly ignorant of the bankruptcy stay' ". *Id.* at 1023. Instead, *Franklin Savings* actually states as follows:

> While district courts and bankruptcy courts have the authority to "annul" a stay, 11 U.S.C. § 362(d), thereby reinstating previous claims retroactively, such a *result is rare* and probably available only to claimants who are honestly ignorant of the bankruptcy case.

Id. (emphasis provided).

Thus, the authorities on which Stallings rely support Spring Meadows' argument and authorities cited in its Petition that retroactive annulment requires a higher standard which is satisfied only in limited circumstances which do not exist here. Moreover, even if some cases support Stallings' claim that ignorance justifies retroactive annulment, the fact that there is a split as to this important and frequently encountered issue evidences the need for this Court's review.

Similarly, Stallings' argument that retroactive stay relief is appropriate because only Spring Meadows' liability insurance carrier's assets, not Spring Meadows' assets, are at issue is factually incorrect. Stallings' 1991 Motion for Relief from Automatic Stay and the resulting June 1991 order did *not* limit Stallings' claim to the amount of insurance proceeds. Rather, Stallings reserved the right to obtain a judgment for the *full* amount of their claim, including an amount in excess of Spring Meadows' liability insurance. Spring Meadows thus could be subject to an excess judgment which could reach its own assets. This is a far cry from Stallings agreeing to obtain a judgment only up to the amount of the insurance proceeds.

Finally, Stallings incorrectly claim there is no reason for the bankruptcy court or Arizona state courts to require that Stallings refile a second identical complaint in this case. To the contrary, to treat a stay violation the same as a nonviolation treats with impunity claimants who violate the automatic stay. Moreover, it

is only a nominal burden for a creditor to simply refile its claim, particularly in light of bankruptcy code § 108(c)'s savings provision. This statutory structure evidences Congressional intent requiring the refiling of a complaint when the stay is violated. The Arizona Supreme Court's *Stallings* decision thus adds to the confusion as to when retroactive stay relief is appropriate.

CONCLUSION

Petitioner Spring Meadows respectfully requests that this Court grant a Writ of Certiorari to resolve these frequently encountered, important and disputed issues of federal law.

Respectfully submitted,

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